



## SENATE BILL 97: Clarify Refunds of Tax Overpayments

2011-2012 General Assembly

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<b>Committee:</b>	Senate Finance	<b>Date:</b>	February 23, 2011
<b>Introduced by:</b>	Sens. Rucho, Hartsell, Daniel	<b>Prepared by:</b>	Trina Griffin
<b>Analysis of:</b>	First Edition		Committee Counsel

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**SUMMARY:** *Senate Bill 97 clarifies when the Department of Revenue is required to initiate a refund of an overpayment of tax and directs the Department to issue refunds for overpayments that have been discovered within the statute of limitations consistent with this clarification.*

**CURRENT LAW:** Generally speaking, there are two methods for obtaining a refund of tax from the Department of Revenue. If a taxpayer is aware that he or she has made an overpayment, then the taxpayer may request a refund by filing an amended return or by filing a claim for refund. If the taxpayer is not aware of the overpayment, the Department is required to initiate the refund process if, within the statute of limitations period, it becomes aware of or "finds" the overpayment.

Specifically, the Department is required to initiate a refund of an overpayment of tax when the Department processes a return and finds all of the following:

1. The statute of limitations for obtaining a refund has not expired.
2. The amount shown due on the return is not correct.
3. The correction of the amount due shows that the taxpayer has overpaid the tax.

The general statute of limitations for obtaining a refund is the later of three years after the due date of the return or two years after the payment of tax.

The current statute does not specify what constitutes "finding" or discovering an overpayment for purposes of satisfying the statute of limitations. In other words, it does not identify what action must take place by the Department before the statute of limitations expires.

**BILL ANALYSIS:** **Section 1** of the bill clarifies when the discovery of an overpayment occurs, which triggers the Department of Revenue's obligation to issue a refund. Discovery occurs in any of the following circumstances:

1. When the automated processing of a return indicates the return requires further review.
2. When a review of a return by an employee indicates an overpayment.
3. When an audit of a taxpayer by an employee indicates an overpayment.

If the Department's computer system flags a return for further review, the Department must still verify that an overpayment exists before issuing a refund because the automated flagging does not always indicate the precise nature of an error on a return. However, this bill clarifies that the verification need not occur within the statute of limitations period. The flagging of the return is sufficient to put the Department on notice that a refund may be due for purposes of satisfying the statute of limitations.

**Section 2** of the bill directs the Department to issue refunds of overpayments that have been discovered within the statute of limitations in a manner consistent with the clarification in Section 1 of the bill. Over the last year, the Department has been working through a backlog of returns that were flagged for review, some dating as far back as 1996. By December 2010, the vast majority of returns had been reviewed and many refunds were issued. However, there remain approximately 7,000 returns in which an overpayment has been made but a refund has not been issued because the Department wants

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clarification from the General Assembly about the application of the current law. These overpayments total a little over \$2 million plus interest.

**EFFECTIVE DATE:** This act is effective when it becomes law.

**BACKGROUND:** The Revenue Laws Study Committee looked at this issue during the recent interim. The Committee heard differing opinions about the interpretation of the law and its application to overpayments. One interpretation is that the Department is required to issue a refund of an overpayment only if the overpayment is verified by a Departmental employee within the statute of limitations period. Under this interpretation, a taxpayer's receipt of a refund is dependent on the Department's ability to timely review the return, which can vary depending on its workload and resources. The other interpretation is that the Department is required to issue a refund of an overpayment if the return is flagged by the Department's computer system within the statute of limitations. The Department may need to verify that an overpayment exists by manual review of a flagged return, but the manual review need not occur within the statute of limitations. Because returns are processed by the computer system almost immediately after they are filed, this interpretation assures that taxpayers will eventually get a refund.

The Committee concluded that when a return is flagged by the computer system, sufficient notice is provided to the Department that a refund may be due.

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